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What FINRA Can Learn from Major League Baseball

Ben Einbinder*

I. INTRODUCTION

For over 150 years, baseball has captivated Americans and has cemented its place as the national pastime.¹ When the game was invented in the early decades of the nineteenth century, it was played “on a strictly amateur basis.”² By the mid-1850s, the baseball craze hit the New York metropolitan area, and professionalism inevitably found its way into the sport.³

In 1869, the Cincinnati Red Stockings became the first fully professional baseball club, and the National Association of Base Ball Players became the sport’s first professional league in 1871.⁴ In 1875, The National Association of Base Ball Players became the National League of Baseball Clubs, the predecessor of today’s National League.⁵ Since the 1870s, professional baseball’s rising popularity, combined with the implementation of free agency and arbitration, has turned the game into a multibillion-dollar industry.⁶ Today, Major League Baseball (MLB) consists of thirty teams made up of over 700 players.⁷ Over the years, MLB has dealt with its fair share of employment disputes.

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1. Kevin A. Rings, *Baseball Free Agency and Salary Arbitration*, 3 OHIO ST. J. ON DISP. RESOL. 243, 244 (1987).

2. *See id.*

3. BENJAMIN G. RADER, *BASEBALL: A HISTORY OF AMERICA’S GAME* 9 (3d ed. 2008).

4. DEAN SULLIVAN, *EARLY INNINGS: A DOCUMENTARY HISTORY OF BASEBALL, 1825–1908*, 73-87 (1997). The National Association of Base Ball Players lasted from 1871 to 1875. *Id.* at 83-84.

5. *See Rings, supra* note 1, at 244.

6. *See* Nancy Kercheval, *Major League Baseball Revenue Reaches Record, Attendance Falls*, BLOOMBERG (Oct. 1, 2008, 9:13 PM), <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=asFEMjfiKA5s>.

7. *See Complete Baseball Team and Baseball Team Encyclopedias*, BASEBALL-REFERENCE.COM, <http://www.baseball-reference.com/teams> (last visited Mar. 6, 2012). There are 30 teams with 25 players on each team. *Id.*

The securities industry is no different, and in 1986 the securities employment arbitration program was established.⁸ In the first twelve years of the program, roughly 3,200 employment awards were issued.⁹ In 2007, the Financial Industry Regulatory Authority (FINRA) was established and assumed control of the dispute resolution programs formerly administered by the National Association of Securities Dealers (NASD) and the New York Stock Exchange (NYSE).¹⁰

“[FINRA] is the largest independent regulator for all securities firms doing business in the United States.”¹¹ FINRA has over 3,000 employees that oversee nearly 4,500 brokerage firms, about 163,470 branch offices, and approximately 634,385 registered securities representatives.¹² In the securities industry in the United States, FINRA administers the largest dispute resolution forum for investors and registered firms.¹³

This article analyzes MLB’s final-offer arbitration system (the arbitration system) and advocates for its adoption in employment disputes in the finance industry. Part II discusses the history and evolution of the arbitration system. Part III analyzes the current state of the arbitration system and Part IV discusses its effects on player salaries and the implications of those affects on MLB organizations. Part V discusses criticisms of the arbitration system, while Part VI discusses defenses of the system. Part VII examines FINRA’s arbitration model for disputes in the securities industry. Part VIII advocates for the use of final-offer arbitration to determine the amount of the awards for employment disputes in the securities industry. Lastly, Part IX discusses the impact of implementing final-offer arbitration in FINRA employment disputes.

II. HISTORY AND EVOLUTION OF FINAL-OFFER ARBITRATION

In 1879, following a dispute over a uniform, Jim O’Rourke decided to quit the Boston Beaneaters and sign on with the Providence team.¹⁴ In response, the owners of the major league teams met secretly and devised the

8. David B. Lipsky, Ronald L. Seeber & J. Ryan Lamare, *The Arbitration of Employment Disputes in the Securities Industry: A Study of FINRA Awards, 1986-2008*, J. DISP. RES., Feb.-Apr. 2010, at 54.

9. *See id.*

10. *See id.*

11. *About the Financial Industry Regulatory Authority*, FINRA.ORG, <http://www.finra.org/AboutFINRA> (last visited Mar. 6, 2012) [hereinafter FINRA].

12. *Id.*

13. *Id.*

14. *See Rings, supra* note 1, at 245.

“reserve system” to prevent players from “jumping” from team to team.¹⁵ Initially, the reserve system was simply a gentlemen’s agreement between owners that allowed each owner to produce a list of players that were “off-limits” to the rest of the league.¹⁶ Several years later, the reserve system was formalized and a “reserve clause” was written into the contracts of all professional baseball players.¹⁷ Under the reserve system, if a player had a reserve clause in his contract, he was bound to that team for the duration of the contract and the succeeding season as well.¹⁸ If the player had a dispute with his employer, he was unable to seek employment with another team.¹⁹ Many players likened the reserve system to a form of slavery; however, the system satisfied the owners’ desire to retain players as long as they were of value to the team, while also maintaining the freedom to release the players when they had lost their value.²⁰

The reserve system gave the owners complete leverage over of the players. The unrest surrounding the reserve system led to three separate legal challenges, all of which made it to the U.S. Supreme Court.²¹ In *Federal Baseball Club of Baltimore v. National League of Professional Baseball Clubs*, the reserve clause was challenged by a rival league which was attempting to lure players away from the National League.²² Justice Holmes accepted the argument by the National League that the reserve system was a necessity, and upheld the legality of the system.²³ Justice Holmes further held that the reserve clause did not violate antitrust laws because baseball was not a business engaging in interstate commerce.²⁴

15. *See id.*

16. *See id.*

17. *See id.*

18. *See id.* at 246.

19. *See id.* The only alternatives available to players were to accept whatever offer was made by the owner, hope for a trade, or seek employment outside of baseball. *Id.*

20. *See id.*

21. *Flood v. Kuhn*, 407 U.S. 258 (1972); *Toolson v. N.Y. Yankees*, 346 U.S. 356 (1953); *Fed. Baseball Club of Balt., Inc. v. Nat’l League of Prof’l Baseball Clubs*, 259 U.S. 200 (1922).

22. *Fed. Baseball*, 259 U.S. at 207.

23. *See Rings, supra* note 1, at 247.

24. *Fed. Baseball*, 259 U.S. at 208-09.

The business is giving exhibitions of base ball, which are purely state affairs. It is true that in order to attain for these exhibitions the great popularity that they have achieved, competitions must be arranged between clubs from different cities and States. But the fact that in order to give the exhibitions the Leagues must induce free persons to cross

The second legal challenge to the reserve system came in *Toolson v. New York Yankees*.²⁵ In *Toolson*, Earl Toolson objected to the reserve system because he was being assigned to different minor league teams within the Yankees organization and he believed he had a better chance making a major league roster elsewhere.²⁶ The Court relied heavily on *Federal Baseball* and affirmed baseball's exemption from the antitrust laws.²⁷

Following the *Toolson* decision, the players voted to unionize, leading to the creation of the Major League Baseball Players Association (MLBPA) in 1954.²⁸ Although the reserve system remained in place, the MLBPA began addressing issues like the pension fund, minimum salary, and player grievances under its first permanent, full-time director, Marvin Miller.²⁹

By 1967, the MLBPA persuaded the owners to form their own labor relations organization, the Player Relations Committee (PRC), to engage in collective bargaining with the union.³⁰ In 1968, the MLBPA and the PRC created the 1968 Basic Agreement (Agreement), a landmark event in the history of baseball's labor relations.³¹ Among other things, the Agreement increased the minimum salary by \$4,000; whereas, the minimum salary had only increased \$2,000 in the twenty years prior to Marvin Miller's hiring in 1966.³² The Agreement also created the right to formal grievance arbitration

state lines and must arrange and pay for their doing so is not enough to change the character of the business.

Id.

25. *Toolson v. N.Y. Yankees*, 346 U.S. 356 (1953).

26. *Toolson v. N.Y. Yankees*, 101 F. Supp. 93, 93 (S.D. Cal. 1951).

27. *Toolson*, 346 U.S. at 357.

The present cases ask us to overrule the prior decision and, with retrospective effect, hold the legislation applicable. We think that if there are evils in this field which now warrant application to it of the antitrust laws it should be by legislation. Without re-examination of the underlying issues, the judgments below are affirmed on the authority of *Federal Baseball Club of Baltimore v. National League of Professional Baseball Clubs*, *supra*, so far as that decision determines that Congress had no intention of including the business of baseball within the scope of the federal antitrust laws.

Id.

28. Daniel C. Glazer, *Can't Anybody Here Run This Game? The Past, Present and Future of Major League Baseball*, 9 SETON HALL J. SPORT L. 339, 341 (1999).

29. *See id.* at 343-44.

30. LEE LOWENFISH, *THE IMPERFECT DIAMOND: A HISTORY OF BASEBALL'S LABOR WARS* 203 (revised ed. 1991).

31. *Id.*

32. *Id.*

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and it created the Uniform Player's Contract—the standard employment contract signed by all major league players—which could only be changed through collective bargaining.³³

The 1970 Basic Agreement reconfigured the arbitration process requiring a tripartite panel comprised of two partisan members and one neutral, who acted as the Chairman.³⁴ The panel was given jurisdiction to resolve all disputes involving any agreement between “a Player and a Club,” and its rulings were legally binding on both sides.³⁵

The final legal challenge to the reserve system came in 1972 in *Flood v. Kuhn*.³⁶ Curt Flood had been traded by the St. Louis Cardinals to the Philadelphia Phillies and he refused to report to the Phillies.³⁷ Since the *Toolson* decision, there had been other forms of sports and entertainment determined not to be exempt from the antitrust laws;³⁸ however, the Supreme Court again ruled that baseball was unique and was exempt from the antitrust laws, affirming the legality of the reserve system.³⁹

Despite their legal victory in *Flood*, the owners believed that congressional intervention was imminent and, as such, were more willing to compromise on changes to the reserve system in the 1973 Basic Agreement.⁴⁰ The most significant concession was final-offer arbitration for salary disputes of all players with more than two years of major league service.⁴¹ The first salary arbitration hearing took place on February 11, 1974 between pitcher Dick Woodson and the Minnesota Twins.⁴²

33. *Id.* The Commissioner decided the grievances. *Id.* Ultimately, the impartiality was questioned because the owners paid the Commissioner. *Id.* See also MARVIN MILLER, A WHOLE DIFFERENT BALL GAME: THE SPORT AND BUSINESS OF BASEBALL 97 (1991).

34. Basic Agreement, art. X (1970), available at <http://www.bizofbaseball.com/docs/1970CBA.pdf>.

35. *Id.*

36. *Flood v. Kuhn*, 407 U.S. 258 (1972).

37. *Id.* at 265.

38. See Rings, *supra* note 1, at 249.

39. *Flood*, 407 U.S. at 285.

40. Glazer, *supra* note 28, at 351.

41. Daniel R. Marburger, *Whatever Happened to the “Good Ol’ Days”?*, in STEE-RIKE FOUR!: WHAT’S WRONG WITH THE BUSINESS OF BASEBALL 7, 11 (Daniel R. Marburger ed., 1997). Prior to implementing final-offer arbitration, the player’s only leverage was to hold out into the season or retire. *Id.* Final-offer arbitration allowed the player and the club to submit their best offers to a neutral arbitrator following an impasse in negotiations. *Id.* The arbitrator would then decide between the two offers. *Id.*

42. Ed Edmonds, *A Most Interesting Part of Baseball’s Monetary Structure—Salary Arbitration in its Thirty-Fifth Year*, 20 MARQ. SPORTS L. REV. 1, 1 (2009). Woodson won his

Following the 1973 Agreement, there were several grievances that would end up changing the game forever. Prior to the 1974 season, Jim “Catfish” Hunter signed a one-year, \$100,000 contract with the Oakland Athletics.⁴³ Hunter requested that half of the amount be paid as regular salary and the other half be used to purchase a \$50,000 non-taxable annuity in Hunter’s name.⁴⁴ However, the club owner, Charles Finley, refused Hunter’s request because the payment would not be tax-deductible for Finley until Hunter collected on the annuity.⁴⁵ As a result, the MLBPA filed a grievance on behalf of Hunter claiming that Finley’s refusal to purchase the annuity voided Hunter’s playing contract.⁴⁶ In December 1974, arbitrator Peter Seitz ordered Finley to purchase Hunter’s annuity and declared Hunter free to contract with any club he wished.⁴⁷ Hunter then signed an unprecedented five-year, \$3.75 million contract with the New York Yankees.⁴⁸ The result of the arbitration was a revelation among the other players of their true market value.

In early 1974, Andy Messersmith signed a \$90,000, one-year contract with the Los Angeles Dodgers and had an exceptionally good season.⁴⁹ The following year, Messersmith requested a “no-trade” provision in his contract but was refused when the Dodgers unilaterally renewed his contract under Section 10(a) of the Uniform Player’s Contract.⁵⁰ The MLBPA filed a grievance on behalf of Messersmith and Montreal Expos pitcher Dave McNally following the 1975 season, claiming that Section 10(a) only granted teams a one-year renewable option, after which players were free to negotiate with other teams.⁵¹ Despite being encouraged to settle by the arbitration panel, the owners ignored the suggestion and the panel ruled in favor of Messersmith and McNally.⁵² The ruling effectively granted free

hearing when the arbitrator chose his \$30,000 offer instead of the Twins’ \$23,000 offer. *Id.* Woodson was then traded to the New York Yankees where he was sent down to the minor leagues and never returned to the major leagues. *Id.* Woodson claimed he was “blackballed” because he used the arbitration process. *Id.*

43. See MILLER, *supra* note 33, at 227.

44. See *id.*

45. See *id.* at 228.

46. See *id.* at 231.

47. See *id.* at 233.

48. See *id.* at 237.

49. See *id.* at 241.

50. *Id.* Section 10(a) provided, in relevant part: “If prior to the [beginning of the season], the Player and the Club have not agreed upon the terms of [a] contract, . . . the club shall have the right . . . to renew this contract for the period of one year on the same terms” Uniform Player’s Contract, § 10(a) (1973) (incorporated as an appendix to the 1976 Basic Agreement).

51. See Glazer, *supra* note 28, at 353-54.

52. See *id.* at 355.

agency without a minimum service requirement as a player simply had to refuse to sign a new contract following the expiration of his previous contract, play out his option year, and become a free agent at the end of the season.⁵³

The Messersmith-McNally decision led to immediate changes to the structuring of the reserve system in the 1976 Basic Agreement.⁵⁴ Under the new system, teams could reserve players with fewer than six years of major league service.⁵⁵ After six years of major league service, players became free agents and were able to participate in a post-season “re-entry draft.”⁵⁶ Players, however, were limited to bids by up to twelve teams during the draft.⁵⁷ Through the use of arbitration, the Messersmith-McNally decision truly set the stage for exponential growth in player salaries.⁵⁸

The two decades following the Messersmith-McNally decision were filled with conflict between the owners and the MLBPA.⁵⁹ There were player strikes in 1981, 1985, and 1994 and an owners’ lockout in 1990.⁶⁰ The disputes ultimately led to the arbitration structure as it stands today.⁶¹

III. OVERVIEW OF THE CURRENT ARBITRATION SYSTEM

The current salary structure in MLB separates players into three groups depending on major league service.⁶² The first group consists of players that are not yet eligible for arbitration and are bound to one team, similar to the

53. *See id.* at 356.

54. *See id.*

55. Basic Agreement, art. XVII(B) (1976), available at <http://bizofbaseball.com/docs/1976CBARotate.pdf>.

56. *Id.* at art. XVII(B), (C).

57. *Id.*

58. ANDREW S. ZIMBALIST, *BASEBALL AND BILLIONS: A PROBING LOOK INSIDE THE BIG BUSINESS OF OUR NATIONAL PASTIME* 76 (updated ed. 1994). After fifteen years of free agency, the average player in 1991 earned forty-seven times the mean annual U.S. income. *Id.* at 77.

59. *See* Glazer, *supra* note 28, at 358.

60. *See id.* at 358-64.

61. PAUL DICKSON, *THE DICKSON BASEBALL DICTIONARY* 736 (3d ed. 2009).

62. Basic Agreement, art. VI(F)(1) (2007-2011), available at http://mlb.mlb.com/pa/pdf/cba_english.pdf. Major league service is calculated by the number of days a player is on the major league roster in a given year. *Id.* A year in the major leagues is defined as 172 days on the major league roster. *Id.*

reserve system prior to the Messersmith-McNally decision.⁶³ These players are typically paid a salary close to the league minimum.⁶⁴

The second group includes all players that have accrued enough service time to satisfy the requirements to become eligible for arbitration.⁶⁵ Players become arbitration-eligible when they have accrued “a total of three or more years of Major League service, however accumulated, but with less than six years of Major League service.”⁶⁶ A player may also be arbitration-eligible if he has

[A]t least two but less than three years of Major League service . . . if: (a) he has accumulated at least 86 days of service during the immediately preceding season; and (b) he ranks in the top seventeen percent (17%) (rounded to the nearest whole number) in total service in the class of Players who have at least two but less than three years of Major League service, however accumulated, but with at least 86 days of service accumulated during the immediately preceding season.⁶⁷

Once a player becomes arbitration-eligible, he is then able to negotiate his salary with his club.⁶⁸ Upon impasse, the player and the club submit their final offers to an impartial arbitration panel.⁶⁹ The arbitration panel must select one of the two offers submitted and cannot pick an amount in-between.⁷⁰ The Basic Agreement sets forth the criteria the panel may consider when deciding between the offers.⁷¹ The panel’s decision is

63. See Edmonds, *supra* note 42, at 7.

64. See *id.*

65. See *id.*

66. Basic Agreement, art. VI(F)(1) (2007-2011).

67. *Id.* at art. VI(F)(1). This category of players is commonly known in baseball as the “Super Twos.” Edmonds, *supra* note 42, at 7.

68. Edmonds, *supra* note 42, at 7. The arbitration system is the dispute resolution system that the MLBPA and the owners agreed to use when the negotiations reach an impasse. *Id.*

69. See Rings, *supra* note 1, at 254.

70. See *id.*

71. Basic Agreement, art. VI(F)(12)(a) (2007-2011). The criteria includes:

[T]he quality of the Player’s contribution to his Club during the past season (including but not limited to his overall performance, special qualities of leadership and public appeal), the length and consistency of his career contribution, the record of the Player’s past compensation, comparative baseball salaries (see paragraph (13) below for confidential salary data), the existence of any physical or mental defects on the part of the Player, and the recent performance record of the Club including but not limited to its League standing and attendance as an indication of public acceptance (subject to the exclusion stated in subparagraph (b)(i) below).

Id. The panel cannot consider evidence related to the following:

- (i) The financial position of the Player and the Club; (ii) Press comments, testimonials or similar material bearing on the performance of either the Player or the Club, except that

binding on the player and his club only for the season immediately following the hearing.⁷² A player may submit to arbitration up to three times prior to reaching free agency.⁷³

The third group includes all players with at least six years of service who have attained free agent status.⁷⁴ Upon the expiration of a free agent's contract, a club can offer arbitration to the player.⁷⁵ If the player accepts the offer to arbitrate, he is considered a signed player for the next season.⁷⁶ If the player rejects the offer to arbitrate, he then becomes a free agent classified as either a Type A, Type B, or unranked player depending on the statistical rubric set forth in the Basic Agreement.⁷⁷ The classifications determine what level of compensation the player's former club receives as a result of the player's election of free agency.⁷⁸ Once a player has attained free agent status, he is able to seek the highest offer on the open market.⁷⁹

IV. THE AFFECTS OF THE ARBITRATION SYSTEM IN MLB

Since its inception, the implementation of final-offer arbitration has substantially affected MLB. When the owners and the MLBPA included arbitration in the 1973 Basic Agreement, they envisioned a system that

recognized annual Player awards for playing excellence shall not be excluded; (iii) Offers made by either Player or Club prior to arbitration; (iv) The cost to the parties of their representatives, attorneys, etc.; (v) Salaries in other sports or occupations.

Id. It should also be noted that the arbitration panel is not allowed to issue a written opinion of their reasoning behind choosing the offer they chose. *Id.* at art. VI(F)(5).

72. Basic Agreement, art. VI(F) (2007-2011). A club cannot submit an offer less than 80% of the player's previous year's salary unless the player won a salary arbitration in the immediately preceding year which increased the player's prior year's salary by an excess of 50%. *Id.* at art. VI(F)(3)(c)(i)-(ii).

73. *Id.* at art. VI(F).

74. See Edmonds, *supra* note 42, at 8.

75. Basic Agreement, art. XX(B) (2007-2011). The same criteria are used from Article VI. *Id.*

76. *Id.*

77. *Id.* Type A players are those who rank in the upper twenty percent of their respective position group, whereas, Type B players are those who rank in the upper forty percent but not in the upper twenty percent of their respective position group. *Id.* All players not considered Type A or Type B are classified as unranked free agents. *Id.*

78. *Id.*

79. See Edmonds, *supra* note 42, at 8. Inherent in the term "free agent" is the individual player's freedom from any team.

would lead to fewer disputes and more settlements.⁸⁰ The parties chose final-offer arbitration because the high level of risk inherent in the all-or-nothing procedure incentivizes parties to negotiate in good faith and settle prior to a hearing.⁸¹ The theory behind final-offer arbitration is that it promotes a “convergence” of the two positions in the arbitration as the parties will make concessions to make their offers more reasonable to the arbitration panel.⁸² The two sides are ultimately more likely to bargain in hopes of reaching an agreement prior to the hearing if they fear that the arbitrator may view the other side’s offer as more reasonable.⁸³

Statistically, MLB’s arbitration system has accomplished its goals. Since arbitration was incorporated into the 1973 Basic Agreement, 84.32% of salary arbitration cases filed settled prior to actually being arbitrated.⁸⁴ Only twice has the number of arbitrations heard exceeded 50% of the cases filed.⁸⁵ In 2009, more than 97% of the arbitration-eligible players settled prior to a hearing.⁸⁶

Along with an increase in the number of settlements, player salaries have also increased since the introduction of arbitration. In fact, the average annual negotiated settlement between 1974 and 1993 resulted in a gain ranging from 33% to 110% over the previous year’s salary.⁸⁷ In 1993, players who prevailed in their arbitration hearings gained a 174% salary increase, whereas players who “lost” averaged a 54% increase in salary.⁸⁸ As a result, teams have started negotiating multiyear contracts for highly talented players to avoid the arbitration process.⁸⁹ This allows teams to

80. Thomas J. Hopkins, *Arbitration: A Major League Effect on Players’ Salaries*, 2 SETON HALL J. SPORT L. 301, 306 (1992).

81. Adam Primm, Note, *Salary Arbitration Induced Settlement in Major League Baseball: The New Trend*, 17 SPORTS LAW. J. 73, 87 (2010).

82. *See id.* at 88.

83. Jonathan M. Conti, *The Effect of Salary Arbitration on Major League Baseball*, 5 SPORTS LAW. J. 221, 231 (1998).

84. *See* Primm, *supra* note 81, at 92.

85. *See id.* The only two years were 1974 and 1978. *Id.*

86. Maury Brown, *Detailed Report: 2009 MLB Salary Arbitration by Club, Position, and More*, THE BIZ OF BASEBALL (Feb. 24, 2009, 12:54 PM), http://www.bizofbaseball.com/index.php?option=com_content&view=article&id=2982:detailed-report-2009-mlb-salary-arbitration-by-club-position-and-more&catid=66:free-agency-and-trades&Itemid=153. Only three of the 111 arbitration-eligible players failed to settle prior to a hearing. *Id.*

87. *See* Conti, *supra* note 83, at 235.

88. Vittorio Vella, Comment, *Swing and a Foul Tip: What Major League Baseball Needs to Do to Keep Its Small Market Franchises Alive at the Arbitration Plate*, 16 SETON HALL J. SPORTS & ENT. L. 317, 326 (2006).

89. *See* Primm, *supra* note 81, at 93. In 2009, 15 of the 111 players who filed for arbitration received multiyear contracts in lieu of the one-year contract that typically results from arbitration.

negotiate with players before they have reached their full playing potential and, thus, their full earning potential.⁹⁰ However, the arbitration system has forced teams to bear the risk of declining future performance or injury or face the potential annual salary increases associated with arbitration.⁹¹

V. CRITICISMS OF MLB'S ARBITRATION SYSTEM

Critics of MLB's arbitration system tend to focus on the damaging effects the increase in player salaries has had on the game.⁹² First, they note that final-offer arbitration disproportionately favors player interests.⁹³ Arbitration-eligible players receive an increase in their salaries regardless of whether or not they prevail in their hearings.⁹⁴ In 2009, the average increase in salary among arbitration-eligible players was 143%.⁹⁵

Another criticism of the arbitration system is that the differential between player offers and team offers has widened greatly since the system's inception.⁹⁶ In 1974, player offers were 20% higher than their team offers.⁹⁷ In 1993, however, player offers jumped to 63% higher than team offers.⁹⁸ The divergence of offers has made the high-risk procedure even more unpredictable.⁹⁹

Benjamin A. Tulis, *Final-Offer "Baseball" Arbitration: Contexts, Mechanics & Applications*, 20 SETON HALL J. SPORTS & ENT. L. 85, 91 (2010).

90. See Primm, *supra* note 81, at 93.

91. See *id.* at 97. The player also bears the risk that his market value will increase beyond the value of his multiyear contract as he continues to develop his talent. *Id.*

92. See generally Vella, *supra* note 88; Josh Chetwynd, *Play Ball? An Analysis of Final-Offer Arbitration, Its Use in Major League Baseball and Its Potential Applicability to European Football Wage and Transfer Disputes*, 20 MARQ. SPORTS L. REV. 109 (2009); Bibek Das, *Salary Arbitration and the Effects on Major League Baseball and Baseball Players*, 1 DEPAUL J. SPORTS L. & CONTEMP. PROBS. 55 (2003); John P. Gillard, Jr., Note, *An Analysis of Salary Arbitration in Baseball: Could a Failure to Change the System be Strike Three for Small-Market Franchises?*, 3 SPORTS LAW. J. 125 (1996).

93. See Vella, *supra* note 88, at 326.

94. See Das, *supra* note 92, at 57.

95. See Chetwynd, *supra* note 92, at 132.

96. See Gillard, *supra* note 92, at 131. Player offers have increased at a much higher rate than team offers since the implementation of arbitration. *Id.*

97. See *id.*

98. See *id.*

99. See *id.* at 132.

Final-offer arbitration has also been criticized because of the adversarial nature of the proceeding.¹⁰⁰ When advocating for their offer, teams are forced to disclose degrading and detrimental evidence of the player's character and conduct to persuade the arbitration panel to accept their offer.¹⁰¹ Players may feel betrayed following an arbitration hearing, regardless of the outcome, and may perform below their potential as a result.¹⁰² The detrimental effects to the relationship may cause players to refuse to re-sign with the team during their free agency years or even request a trade during the upcoming season.¹⁰³

Finally, opponents of the MLB arbitration system have criticized the system because of the way it has enlarged the disparity between small- and large-market teams.¹⁰⁴ Arbitrators are not able to consider the financial status of the player or the team when making their decision.¹⁰⁵ Large-market teams, however, are typically willing to pay higher free agent salaries than small-market teams, and these salaries are taken into consideration in arbitration hearings.¹⁰⁶ Therefore, MLB's arbitration system imposes an economic loss on small-market franchises by forcing them to sign players for salaries exceeding their value to the team.¹⁰⁷

VI. DEFENSES OF MLB'S ARBITRATION SYSTEM

Proponents of MLB's arbitration system highlight the fact that arbitration works quickly and fairly while encouraging "parties to adopt a realistic, good faith bargaining position."¹⁰⁸ Even opponents to arbitration cannot deny that the program has encouraged pre-arbitration settlements. Since 1988, 89.23% of salary arbitration cases have settled prior to a hearing.¹⁰⁹

Supporters of arbitration argue that MLB's arbitration system should not be blamed for the increases in player salaries.¹¹⁰ In recent years, the average

100. See Das, *supra* note 92, at 58.

101. See *id.*

102. See *id.*

103. See *id.*

104. See Gillard, *supra* note 92, at 134.

105. Basic Agreement, art. VI(F) (2007-2011).

106. See Vella, *supra* note 88, at 328.

107. See *id.*

108. Frederick N. Donegan, *Examining the Role of Arbitration in Professional Baseball*, 1 SPORTS LAW. J. 183, 204 (1994). The arbitrators must reach a decision no later than twenty-four hours following the close of the hearing. Basic Agreement, art. VI(F) (2007-2011).

109. See Primm, *supra* note 81, at 92.

110. Matt Mullarkey, Note, *For the Love of the Game: A Historical Analysis and Defense of Final Offer Arbitration in Major League Baseball*, 9 VA. SPORTS & ENT. L.J. 234, 247 (2010).

player salary has exceeded the average arbitration award.¹¹¹ This suggests that salary increases should be attributed to a combination of arbitration and free agency.¹¹² Some commentators suggest that if either free agency or arbitration had been implemented independently of the other, player salaries would not have increased as dramatically.¹¹³ Arbitration backers also attribute the increase in salaries resulting from arbitration to the fact that players are underpaid during their first three seasons in the major leagues.¹¹⁴

With respect to the small-market teams, advocates of arbitration argue that the system actually benefits those teams.¹¹⁵ Arbitration allows small-market teams to negotiate multiyear contracts without the threat of losing their better players to other teams through free agency.¹¹⁶ Multiyear contracts allow small-market teams to hold on to a player into his early years of free agency while paying him less than his free agent market value.¹¹⁷

Many of the benefits of MLB's arbitration system are a product of the system's final-offer structure. If similar arbitration schemes were utilized in other industries, like the securities industry, the benefits would likely follow.

VII. OVERVIEW OF THE FINRA EMPLOYMENT DISPUTE RESOLUTION PROGRAM

In the securities industry, Rule 13200 of the Code of Arbitration Procedure for Industry Disputes requires a dispute to be arbitrated if it "arises out of the business activities of a 'member' or an 'associated person' and is between or among members, associated persons, or members and associated persons."¹¹⁸ Members are brokers and dealers, and the employees

111. *See id.* at 248.

112. *See* Gillard, *supra* note 92, at 133.

113. *See id.* Abolishing arbitration would create an increase in the supply of free agent players each season. *Id.* According to basic economic principles, an increase in the supply would cause the market price of free agents to decrease. *Id.* Implementing arbitration without free agency would have restricted the open market causing salaries to decrease. *Id.*

114. *See* Primm, *supra* note 81, at 107. A player's salary during his first year of arbitration eligibility should be viewed not just as compensation for the upcoming season, but also as the compensation he should have received during his first three seasons. *See* Mullarkey, *supra* note 110, at 248.

115. *See* Mullarkey, *supra* note 110, at 249.

116. *See id.*

117. *See id.* Young players have a large incentive to accept a multiyear agreement because of the day-to-day risks involved with playing baseball. *Id.* The average MLB career only lasts a little more than five years. *Id.*

118. *See* Lipsky, Seeber & Lamare, *supra* note 8, at 54.

in FINRA employment cases are brokers registered with the Securities and Exchange Commission (SEC).¹¹⁹ These employees are authorized to recommend and execute buy-sell orders, known as registered representatives.¹²⁰

FINRA arbitrations commence when an employee files an initial statement of claim with the Director of FINRA Dispute Resolution.¹²¹ The arbitration then proceeds similar to a traditional court proceeding, allowing the respondent to provide an answer to the claim or file a motion to dismiss the arbitration.¹²² Following the initial filings, the parties are able to select the arbitrators through a process of striking and ranking the arbitrators on lists generated by a computer system.¹²³ Once the arbitrators have been selected, the parties participate in a prehearing conference to set the ground rules for the case.¹²⁴ Unless the parties settle, withdraw, or the case has been dismissed, the case will then proceed to a hearing.¹²⁵ The arbitration panel is required to provide a written decision and is given full discretionary power when deciding the arbitration award.¹²⁶ Following a decision, parties to FINRA arbitration cases may have the arbitration award vacated under certain circumstances.¹²⁷

119. *See id.*

120. *See id.*

121. FINRA CODE OF ARBITRATION PROCEDURE FOR INDUS. DISPUTES R. 13300 (2011). The FINRA rules require that claims be filed within six years of the occurrence or event giving rise to the claim. *Id.* at R. 13206.

122. *Id.* at R. 13302-14.

123. *Id.* at R. 13400.

124. *Id.* at R. 13500. During the prehearing conference, the arbitration panel typically sets discovery, briefing, deadlines for motions, scheduling for subsequent sessions, and other preliminary matters. *Id.*

125. *Id.* at R. 13600. The parties may also elect a simplified arbitration proceeding if the arbitration involves a claim under \$25,000. *Id.* at R. 13800. The simplified arbitrations are administered by a single arbitrator and no hearings are held unless requested by one of the parties. *Id.* There is also an expedited procedure for cases involving a claim that an associate failed to pay money owed on a promissory note. *Id.* at R. 13806.

126. *Id.* at R. 13904.

127. 9 U.S.C. § 10 (2009). Circumstances include:

(1) where the award was procured by corruption, fraud or undue means; (2) where there was evident partiality or corruption in the arbitrators, or either of them; (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; (4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

Id.

Between 1986 and 2008, the FINRA arbitration cases can be separated into five categories: (1) cases where employees claimed the employer denied them compensation allegedly owed; (2) cases where employees claimed the employer had defamed them in some fashion; (3) cases where employees claimed they were wrongfully terminated; (4) cases where employees claimed their employer breached the contract; and (5) cases where employees made a claim of statutory discrimination against the employer.¹²⁸ Every case involved the employee presenting the arbitrator with a monetary figure and the employer taking the position that the arbitrator should not award the employee any money at all.¹²⁹

Employees were awarded a monetary amount in 61% of the cases, and the average award across all cases was nearly \$146,000.¹³⁰ The average, however, is elevated because there were a handful of large awards given during this period.¹³¹ In fact, one employee was awarded over \$27 million in 2001.¹³² However, this case was an anomaly as the median amount claimed in FINRA arbitrations was \$375,000, and the median amount awarded was only \$1,000.¹³³ Employee awards were greater than 50% of what they claimed only 20% of the time.¹³⁴

The FINRA arbitration process has proven to be time consuming as the average amount of time between the filing of the claim and the issuance of an award was about seventeen months.¹³⁵

VIII. A CASE FOR FINAL-OFFER ARBITRATION IN FINRA EMPLOYMENT DISPUTES

Employment arbitrations in FINRA can logically be split into two processes: determining liability and determining the amount of the award.¹³⁶

128. See Lipsky, Seeber & Lamare, *supra* note 8, at 55. The distribution of cases was 28%, 27.4%, 13.5%, 8.4%, and 17.1% respectively. *Id.* Pursuant to the FINRA rules, however, statutory employment discrimination claims are not required to be arbitrated. FINRA CODE OF ARBITRATION PROCEDURE FOR INDUS. DISPUTES R. 13201 (2011).

129. See Lipsky, Seeber & Lamare, *supra* note 8, at 55.

130. See *id.*

131. See *id.*

132. See *id.*

133. See *id.*

134. See *id.* at 57.

135. See *id.*

136. Interview with Robert A. Uhl, Attorney and Arbitrator, Aidikoff, Uhl & Bakhtiari, in Beverly Hills, Cal. (Feb. 23, 2011). Mr. Uhl has appeared on Fox News and has been quoted on

In cases where liability is found, the majority of the time is spent determining the amount of the award.¹³⁷ This article advocates for requiring the use of final-offer arbitration only to determine the amount of the award.¹³⁸

Employment disputes in the securities industry are ripe for the use of final-offer arbitration for several reasons. First, final-offer arbitration will incentivize claimants to make more reasonable claims once liability has been found.¹³⁹ Between 1986 and 2008, the median amount awarded in FINRA employment cases was only a quarter of a percent of the amount claimed.¹⁴⁰ The high risk nature of final-offer arbitration would force parties to re-evaluate what their cases are really worth before submitting their final offers to the arbitration panel.¹⁴¹ If a party truly believes he has a strong case, the process should not affect his offers.

Adopting final-offer arbitration would also increase the rate of settlement in FINRA employment disputes.¹⁴² By forcing parties to submit more reasonable offers, the system creates a more realistic bargaining zone.¹⁴³ In turn, this would promote more settlements due to the risk involved with requiring the arbitration panel to select one party's offer or the other.¹⁴⁴ Again, parties who believe they have a strong case will not be deterred from presenting their award amount to the arbitration panel.¹⁴⁵

Another major benefit of using final-offer arbitration would be a decrease in the costs of arbitration.¹⁴⁶ While a direct application of the MLB timetable may not be appropriate,¹⁴⁷ as FINRA cases may present more

securities matters by The Wall Street Journal, Registered Representative magazine, MarketWatch, and other members of the national and local press. *Id.* Mr. Uhl was also recognized as a 2005, 2006, 2007, 2008, 2009, 2010, and 2011 Southern California Super Lawyer. *Id.* The majority of Mr. Uhl's experience with FINRA arbitrations is in investor arbitrations. *Id.*

137. *Id.*

138. Currently, parties have the choice to settle their case at any time throughout the arbitration process. FINRA CODE OF ARBITRATION PROCEDURE FOR INDUS. DISPUTES R. 13701 (2011). Parties can also choose to use final-offer arbitration if both sides are in agreement. *Id.* at R. 13105.

139. See Rings, *supra* note 1, at 255 ("The practical effect of this system is that both sides have incentive to keep the figures they submit within reason. If one proposal is too extreme, the other wins almost by default.").

140. See Lipsky, Seeber & Lamare, *supra* note 8, at 56.

141. See Primm, *supra* note 81, at 87.

142. See *id.* at 91.

143. See *id.* at 82.

144. In 2009, only 3% of the MLB arbitration cases went to a hearing. Brown, *supra* note 86.

145. See Primm, *supra* note 81, at 87.

146. Presumably, less time spent in arbitration will lead to lower costs.

147. Parties in MLB arbitration are required to submit their offers between January 5 and January 15 of the given year. Basic Agreement, art. VI(F) (2007-2011). The hearings are then scheduled to be held between February 1 and February 20 with a decision coming within twenty-

complex claims, the arbitration process would undoubtedly be expedited by narrowing the arbitration panel's decision to two offers.¹⁴⁸ Expediting the process will lead to a reduction in incidental costs and attorneys fees associated with the arbitration process.¹⁴⁹

The main criticisms of MLB's final-offer arbitration system are specific to issues that are unique to MLB.¹⁵⁰ Therefore, the benefits of adopting mandatory final-offer arbitration in the determination of award amounts would likely outweigh any potential negative consequences.

IX. THE IMPACT OF IMPLEMENTING FINAL-OFFER ARBITRATION IN FINRA EMPLOYMENT DISPUTES

If FINRA adopted the requirement of using final-offer arbitration for employment disputes, there would be a significant impact on the current arbitration system. It is important to understand that adding final-offer arbitration to the current FINRA arbitration program would not lead to a sacrifice in justice. This article does not suggest that final-offer arbitration should be used in the determination of liability.¹⁵¹ Therefore, employers and employees will still be entitled to the same level of procedural due process as the current program.

By limiting the choices for the arbitration panel, the use of final-offer arbitration in the determination of the award amount will reduce the length of the arbitration process. As previously stated, the average FINRA arbitration case took nearly seventeen months from the filing of the claim to the issuance of an award.¹⁵² If employment arbitration cases resemble investor cases, in terms of the amount of time used to determine the amount

four hours following the close of the hearing. *Id.* The maximum amount of time between submitting offers and receiving a decision is never longer than eight weeks. *Id.*

148. Although MLB's exact timetable may not be appropriate, FINRA could impose a similar time limit once liability has been determined. *See supra* note 148.

149. *See* Lipsky, Seeber & Lamare, *supra* note 8, at 56. One case cost a party over \$700,000 in attorney's fees. *Id.* Not to mention the considerable amount of costs incurred by diverting company resources away from day to day tasks.

150. *See supra* Part V. The only criticism that might apply would be the potential for divergence in offers. *See supra* note 100 and accompanying text.

151. It should be noted that the determination of liability is inherently similar to a final-offer arbitration structure. The arbitration panel is forced to decide between two choices: liability or no liability.

152. *See* Lipsky, Seeber & Lamare, *supra* note 8, at 33.

of the award, adopting final-offer arbitration should result in a significant reduction in the overall length of the arbitration.

Another probable impact of requiring final-offer arbitration in the determination of the award amount would be an increase in settlement. The high-risk nature of final-offer arbitration forces parties to realistically evaluate their case and present reasonable offers to the arbitration panel. An increase in realistic offers will ultimately lead to more realistic bargaining zones. In turn, the combination of a high-risk procedure and realistic bargaining zones will lead to increased settlement.¹⁵³

The most significant impact of requiring final-offer arbitration will be decreased costs and expenses. The fundamental characteristics of final-offer arbitration are designed to curtail the length of the arbitration.¹⁵⁴ Reducing the time needed to resolve the dispute will lead to a reduction in the costs of the arbitrators and a reduction in attorneys' fees. Additionally, the excess time and resources being used in arbitration under the current system could be reallocated to benefit both the employer and the employee involved in the case.

Overall, requiring final-offer arbitration in FINRA employment disputes to determine the amount of the award is likely to have a significant, positive impact on the parties involved.

X. CONCLUSION

For nearly forty years, MLB has used final-offer arbitration to resolve salary disputes between players and clubs. MLB's arbitration system has proven to be both efficient and cost effective. While the current FINRA arbitration procedure has proven to be a viable alternative to the traditional litigation process, parties would likely benefit if final-offer arbitration was required in the determination of the award amount. Implementing final-offer arbitration will lead to shorter arbitrations, more settlements, and lower costs, while ensuring justice for those involved.

153. As previously discussed, Major League Baseball has experienced settlement rates over 97% in recent years. Brown, *supra* note 86.

154. The arbitration panel is limited to two choices.